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IN THE UNITED STATES BANKRUPTCY COURT

EASTERN DISTRICT OF CALIFORNIA

FRESNO DIVISION

In re

CASE NO. 17-13797

TULARE LOCAL HEALTHCARE
DISTRICT, dba TULARE
REGIONAL MEDICAL CENTER,

DC No.: LPP-1

Chapter 9

Debtor.

**RESPONSE OF TULARE LOCAL
HEALTHCARE DISTRICT TO MOTION
FOR PAYMENT OF ADMINISTRATIVE
EXPENSES AND AMENDED PROOF
OF CLAIM**

Tax ID #: 94-6002897
Address: 869 N. Cherry Street
Tulare, CA 93274

Date: January 17, 2019
Time: 9:30 a.m.
Place: 2500 Tulare Street
Fresno, CA 93721
Courtroom 13
Judge: Honorable René Lastreto II

Debtor Tulare Local Healthcare District (the "District" or "Debtor") respectfully submits this response ("Response") to the "Motion for Payment of Administrative Expenses and Amended Proof of Claim 188" ("Motion") filed by creditor Owens & Minor, Inc. ("O&M") which seeks an order of this Court for payment and allowance of O&M's asserted administrative claims, as well as allowance of an unsecured claim in the total amount of approximately \$15,500. O&M's Motion should be denied for the reasons set

1 forth below.

2 **I. SUMMARY OF ARGUMENT**

3 O&M requests an order: (a) for payment and allowance of an administrative
4 expense claim of \$11,467.03 for goods allegedly delivered in the 20 days immediately
5 prior to the petition date under Section 503(b)(9) of the Bankruptcy Code (the "Code");
6 (b) allowance and payment of a redemption claim as an administrative claim in the
7 amount of \$1,867.91 under Code § 503(b)(1); and (c) allowance of an unsecured claim
8 in the amount of \$2,135.86. See, Motion at p. 2, Ins. 16-22 and p. 5, Ins. 2-7. Although it
9 is not clear from the Motion itself, however, based on the title of the Motion O&M
10 presumably seeks an order directing the District to pay its alleged claim under Section
11 503(b)(9). O&M's Motion should be denied and any adjudication on the allowance of its
12 claims should be deferred because: (1) O&M's Motion seeking adjudication of the merits
13 and the allowance of its claim is premature, and Code § 904 provides that a court may
14 not issue any order interfering with a chapter 9 debtor's revenues, property, or the use or
15 enjoyment of any income-producing property unless the chapter 9 debtor consents or the
16 plan so provides; (2) there are no necessary costs and expenses of preserving the
17 estate under Code § 503(b)(1)(a) in a chapter 9 case; and (3) even if the Court chooses
18 to adjudicate the merits of O&M's claims, O&M has failed to meet its evidentiary burden
19 to establish its claims as administrative expenses for the reasons set forth herein and the
20 separate Evidentiary Objections to the Declaration of Matthew A. Lesnick filed with this
21 Response.

22 **II. BRIEF STATEMENT OF FACTS**

23 The District filed its emergency petition under chapter 9 on September 30, 2017
24 ("Petition Date") because: (1) its former manager, Health Care Conglomerate Associates
25 ("HCCA"), threatened to cease operations at the hospital known as the Tulare Regional
26 Medical Center ("TRMC") and other medical facilities which would have created a health
27 and safety emergency for patients and the public seeking medical care; and (2) the
28 District first learned it was insolvent on September 28, 2017 when HCCA advised the

1 District that it had a critical liquidity crisis, it was completely out of cash, and it could not
2 fund the entire gross payroll.¹ In light of the District's dire financial crisis and HCCA's
3 threats to cease operations, the District was forced to voluntarily cease operations on or
4 about October 29, 2017 in order to avoid a forced shut down by the California
5 Department of Public Health.

6 In October 2018, just over two months ago, the District reopened TRMC after a
7 nearly year-long closure during which the District made diligent efforts to obtain funding
8 and reach an agreement with a well-established local partner dedicated to providing
9 quality medical services to the District's residents. The District reached an agreement
10 with Adventist Health which allowed it to reopen certain emergency medical services at
11 TRMC in October 2018, and the District anticipates that it will enter into a long-term
12 lease with Adventist Health in the first quarter of 2019 after obtaining a change of
13 ownership approval from the California Department of Public Health which will then allow
14 TRMC to provide a full range of medical services, including obstetrics, pediatrics,
15 neonatal intensive care and elective surgery. At that point, the District believes that it will
16 have the necessary pieces in place to better understand the resources the District will
17 have that may be available to pay claims under a plan of adjustment.

18 O&M asserts that it should be allowed an administrative claim of \$11,467.03 for
19 goods allegedly provided after and during the 20 days prior to the Petition Date.
20 However, O&M has failed to present any admissible evidence to: (a) identify or even
21 describe the goods provided, (b) demonstrate how any such goods were reasonable and
22 necessary to the District's operations or to preserve the District's assets, and (c)
23 establish the date(s) on which such goods were allegedly received by the District. O&M
24 seeks an additional administrative claim as a redemption claim in the amount of
25 \$1,867.91 under Code § 503(b)(1), but O&M has failed to present any admissible
26 evidence to: (a) identify or even describe the goods provided, (b) demonstrate how any
27 such goods were reasonable and necessary to the District's operations or to preserve
28

¹ See, Docket No. 115 at pp. 160-61.

1 the District's assets, and (c) establish the date(s) on which such goods were allegedly
2 received by the District. O&M also seeks allowance of an unsecured claim in the amount
3 of \$2,135.86, and its claim suffers from the same evidentiary defects. For the reasons
4 set forth below, O&M's requests for allowance and payment of any amount should be
5 denied and any decision on the allowance of its claim should be deferred until this Court
6 established procedures for objecting to the allowance of claims and/or the District
7 proposes and confirms its plan of adjustment.

8 III. ARGUMENT

9 A proceeding under chapter 9 of the Bankruptcy Code differs in a number
10 respects from cases filed under chapter 7 or 11. Two of the key differences are
11 limitations on the scope of a bankruptcy court's authority over chapter 9 debtors under
12 Code § 904 and what claims constitute administrative claims.

13 14 A. Courts Do Not Have Jurisdiction Or Authority To Issue Orders 15 That Interfere With The Property, Revenues, Or Use Or Enjoyment Of 16 Income Producing Property Of A Chapter 9 Debtor Unless The 17 Debtor Consents Or It Is Pursuant To A Plan

18 Unless a debtor consents or a plan so provides, Code § 904 limits the court's
19 power and jurisdiction over, among other things, the property and revenues a chapter 9
20 debtor or its use or enjoyment of any income-producing property. 11 U.S.C. § 904; *Ass'n*
21 *of Retired Employees of the City of Stockton v. City of Stockton (In re City of Stockton)*,
22 478 B.R. 8, 13 (Bankr. E.D. Cal. 2012) (Code § 904 bars the court, without the
23 municipality's consent, from interfering with its political or governmental powers, property
24 or revenues, and use or enjoyment of income-producing property); *In re Valley Health*
25 *Sys.*, 429 B.R. 692, 714 (Bankr. C.D. Cal. 2010) ("By virtue of § 904, a debtor in chapter
26 9 retains title to, possession of, and complete control over its property and its operations,
27 and is not restricted in its ability to sell, use, or lease its property.").

28 By expressly limiting a court's authority to interfere with a chapter 9 debtor's
assets, Code § 904 protects the constitutionality of chapter 9 under the Tenth
Amendment.

1 "The bill here recommended for passage expressly avoids any restriction on the
2 powers of the States or their arms of government in the exercise of their
3 sovereign rights and duties. No interference with the fiscal or governmental
4 affairs of a political subdivision is permitted. The taxing agency itself is the only
instrumentality which can seek the benefits of the proposed legislation. No
involuntary proceedings are allowable, and no control or jurisdiction over that
property and those revenues of the petitioning agency necessary for essential
governmental purposes is conferred by the bill"

5 H.R. Rep. No. 95-595, at 264 (1977), reprinted in 1978 U.S.C.C.A.N. 5963, 6222; *United*
6 *States v. Bekins*, 304 U.S. 27, 51 (1938) (expressing approval of the foregoing
7 statements of the Committee on the Judiciary of the House of Representatives in
8 upholding the constitutionality of Chapter X of the Bankruptcy Act under the Tenth
9 Amendment to the United States Constitution). In 1975, Congress further narrowed the
10 power of bankruptcy courts to interfere with a municipal debtor's assets by removing
11 from their discretion the determination of whether or not the assets are "necessary for
12 essential governmental services." See H.R. Rep. No. 94-686, at 18 (1975), reprinted in
13 1976 U.S.C.C.A.N. 539, 556.

14 The District does not consent to any order directing that its property or revenues
15 be used to satisfy O&M's asserted administrative claim, and the District has not yet
16 proposed its plan of adjustment. For these reasons, the court lacks jurisdiction and
17 authority to issue any order directing payment of any asserted administrative claims.

18 **B. It Is Premature for the Court To Consider The Merits Of O&M's**
19 **Claims And Determine Whether Any Such Claims Should Be Allowed**

20 Even if the Court had jurisdiction and authority to issue the order O&M requests
21 for payment of its asserted administrative claims, it is premature to consider the merits
22 of O&M's claims. As of the date of the filing of this Response, this Court has not
23 established procedures for the adjudication of the merits of claims filed in the chapter 9
24 case. Nearly 250 proofs of claim have been filed in this chapter 9 case, and it is critical
25 to the efficient administration of this case that the District not be required to litigate and
26 respond to a motion seeking allowance of each and every claim before it proposes and
27 confirms a plan of adjustment and establishes procedures for the efficient administration
28 of claims as part of its plan of adjustment. This is also essential to preserve the
District's very limited assets and allow it to focus its efforts on the process of reopening

1 TRMC. Just over two months ago, the District reopened TRMC after a nearly year-long
2 closure during which the District made diligent efforts to obtain funding and reach an
3 agreement with a well-established local partner dedicated to providing quality medical
4 services to the residents of the District. After reaching an agreement with Adventist
5 Health to reopen TRMC in October 2018 to provide basic emergency medical services,
6 the District anticipates that it will enter into a long-term lease with Adventist Health in the
7 first quarter of 2019 after obtaining a change of ownership approval from the California
8 Department of Public Health. Once that event occurs, the District believes that it will
9 have the necessary pieces in place to better understand what resources may be
10 available to pay claims under a plan of adjustment. Until these steps are completed and
11 the District files its Disclosure Statement and proposes a Plan of Adjustment, the District
12 believes it is premature, inefficient and unnecessary to litigate the merits of any claims.
13 Indeed, the terms of a plan of adjustment may moot the need for a substantial amount
14 of litigation on the allowance of claims.

15 **C. Bankruptcy Code § 503(b)(1)(A) Does Not Apply in Chapter 9**

16 In a chapter 7 or 11 case, claims arising under Section 503(b)(1)(A) for “the
17 actual, necessary costs and expenses of preserving the estate,” are allowable
18 administrative expenses. In a chapter 9 case, however, administrative claims are not
19 allowable because there is no estate. *Diamond Z Trailer, Inc. v. JZ L.L.C. (In re JZ*
20 *L.L.C.)*, 371 B.R. 412, 419 n.4 (B.A.P. 9th Cir. 2007); *In re City of Vallejo*, 403 B.R. 72,
21 78 n.2 (Bankr. E.D. Cal. 2009); *In re Jefferson County, Ala.*, 484 B.R. 427, 460-61
22 (Bankr. N.D. Ala. 2012). At least two courts have held that there can be no “necessary
23 costs and expenses of preserving the estate” in a case where no estate exists. *In re*
24 *New York City Off Track Betting Corp.*, 434 B.R. 131, 142 (Bankr. S.D.N.Y. 2010) (“Off
25 *Track Betting*”); *In re Texas Wyoming Drilling, Inc.*, 486 B.R. 746, 759 (Bankr. N.D. Tex.
26 2013)(no administrative claim exists where there is no estate to benefit); *In re City of*
27 *San Bernardino*, Dkt. No. 2164 at ¶ 16 at pp. 23-24 and Plan attached as Exhibit A
28 thereto at Article I.B.16. at p. 4 and Article II.A at p. 17 (Bankruptcy court approved plan

1 of adjustment that provided that claims arising under section 503(b)(1)(A) are not
2 allowable administrative expenses).

3 In the *Off Track Betting* case, the court considered motions of several creditors to
4 compel the chapter 9 debtor to pay certain fees that had accrued post-petition. The
5 court rejected the argument that those fees were entitled to administrative priority under
6 Code § 503(b)(1)(A). The court reasoned that because a chapter 9 debtor's property
7 remains its own and does not inure into any bankruptcy estate under Code § 541, there
8 can be no administrative expenses for 'the actual and necessary costs of preserving the
9 estate' as contemplated by Code § 503(b)(1)(A). *Off Track Betting*, 434 B.R. at 142. The
10 court's conclusion is in accord with and required by Code § 904, which prevents
11 bankruptcy courts from exercising jurisdiction over a municipality's use of its revenues
12 without the municipality's consent as discussed in Section A above.

13 The Supreme Court has held that statutes allowing administrative priorities in
14 bankruptcy "must be tightly construed." *Howard Delivery Serv. v. Zurich Am. Ins. Co.*,
15 547 U.S. 651, 667, 126 S. Ct. 2105, 2116 (2006). "[I]f one claimant is to be preferred
16 over others, the purpose should be clear from the statute." *Id.* (quoting *Sampsell v.*
17 *Imperial Paper & Color Corp.*, 313 U.S. 215, 61 S. Ct. 904 (1941)). "We take into
18 account, as well, the complementary principle that preferential treatment of a class of
19 creditors is in order only when clearly authorized by Congress." *Id.* at 655 (citing
20 *Nathanson v. NLRB*, 344 U.S. 25, 29, 73 S. Ct. 80 (1952).) Administrative expenses are
21 narrowly construed in chapter 9 cases. *In re Orange County*, 179 B.R. 195, 201(Bankr.
22 C.D. Cal. 1995).

23 Because the Bankruptcy Code does not expressly provide for the payment of
24 section 503(b)(1)(A) claims in chapter 9 cases, this Court should not read Section
25 503(b)(1)(A) more broadly than the statute's plain meaning. Congress did not clearly
26 authorize a priority for post-petition claims against a chapter 9 debtor. Congress could
27 have done so by stating in Code § 902(1) that "estate" when used in the Bankruptcy
28 Code sections made applicable to chapter 9 means "the debtor," as Congress did with

1 respect to "property of the estate." Alternatively, Congress could have written section
2 503(b)(1)(A) to provide for administrative priority for "the actual, necessary costs and
3 expenses of preserving the debtor and the estate," but Congress limited that provision
4 to claims against the estate. Because there is no estate in chapter 9, Code §
5 503(b)(1)(A) simply does not apply in chapter 9. In light of the constitutional concerns in
6 *Bekins* discussed above that led to Congress to enact section 904 (substantially limiting
7 the jurisdiction of the bankruptcy courts over a chapter 9 debtor's property and
8 revenues), the Court should not expand the reach of section 503(b)(1)(A) unless doing
9 so is "clearly authorized by Congress" and "the purpose of doing so is clear from the
10 statute." See, *Nathanson, supra*, 344 U.S. at 29; *Howard Delivery Service, supra*, 547
11 U.S. at 667. For these reasons, O&M's request for the allowance of an administrative
12 claim for goods allegedly received after the Petition Date should be denied.

13
14 **D. O&M Has Not Established Any Administrative Claim under Code
Section 503(b)(9)**

15 Even if the Court chooses to consider the merits of O&M's claim at this early
16 stage, for the reasons set forth in the Evidentiary Objections to the Declaration of
17 Mathew A. Lesnick filed with this Response, O&M has not submitted admissible
18 evidence to establish that it has an administrative claim under Code § 503(b)(9). The
19 District believes that the issue of whether claims arising under Code § 503(b)(9) are
20 allowable administrative expenses in chapter 9 case is an issue of first impression.

21 Code § 503(b)(9) was added by the 2005 Bankruptcy Abuse Prevention and
22 Consumer Protection Act. The legislative history of § 503(b)(9) "suggests that it was
23 aimed at providing relief to sellers of goods who fail to give the required notice under the
24 reclamation provision of section 546(c)[.]" *In re Brown & Cole Stores, LLC*, 375 BR 873,
25 (9th Cir. BAP 2007), *citing* Shirley S. Cho, *The Intersection of Critical Vendor Orders and*
26 *Bankruptcy Code § 503(b)(9)*, 29 Cal. Bankr. J. 7, 11 (2007), in turn citing
27 BAPCPA, *Pub. L. No. 109-8 at § 1227*. Code § 503(b)(9) allows as an administrative
28 expense "the value of any goods received by the debtor within 20 days before the date

1 of commencement of a case under this title in which the goods have been sold to the
2 debtor in the ordinary course of such debtor's business."

3 While the Bankruptcy Code does not define "goods," some courts have adopted
4 the UCC definition describing "goods" as all things – including specially manufactured
5 goods – that are movable at the time of identification to the contract for sale other than
6 the money in which the price is to be paid. *In re NE Opco, Inc.*, 501 BR 233, 241 (Bankr.
7 D. Del. 2013). Goods are "received" under 503(b)(9) when the debtor or its agent takes
8 physical possession of them. *In re World Imports, Ltd.*, 862 F.3d 338 (3d Cir. 2017).

9 The declaration of Matthew A. Lesnick ("Lesnick Declaration") does not comport
10 with Federal Rule of Evidence 602 because: it does not provide facts sufficient to show
11 that the witness has personal knowledge of: (a) whether any materials or products
12 provided were "goods" within the meaning of Code § 503(b)(9) because no description of
13 any materials or products is provided or other documentation identifying any materials or
14 products, (b) if and when any materials or products were received by the District (instead
15 there is only an inadmissible columns of dates under the headings "Trx Date" and "Due
16 Date" that are not explained in the Lesnick Declaration), and (c) how any materials or
17 products that may have been provided were reasonable and necessary to the District's
18 operations or to preserve the District's assets or the value of such materials or products.
19 Furthermore, Exhibit A is inadmissible because: (a) the Lesnick Declaration provides no
20 foundation supporting Exhibit A or his testimony related to the content of Exhibit A; (b)
21 Exhibit A is hearsay to the extent it is offered to prove its content, and (c) the Lesnick
22 Declaration does not contain facts sufficient to justify the use of a chart or summary to
23 prove the content of voluminous writings that cannot be conveniently examined in court
24 as required by Federal Rule of Evidence 1006. Thus, even if the Court considers the
25 merits of O&M's Motion, it should be denied because there is no admissible evidence to
26 support any claim under Code § 503(b)(9) or Code § 503(b)(1)(a).

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1 **IV. CONCLUSION**

2 For the foregoing reasons, the District respectfully requests that the Court: (a)
3 deny O&M's Request for an order allowing it administrative claims in any amount; (b)
4 defer any adjudication of the merits of O&M's claims until after a plan of adjustment is
5 confirmed and a process is established for objecting to claims; and (c) if the Court
6 chooses to adjudicate the merits of the Motion, deny O&M's requested administrative
7 claims and reclassify such claim as a general unsecured claim.

8
9 Dated: January 2, 2019

WALTER WILHELM LAW GROUP,
a Professional Corporation

10
11 By: Riley C. Walter
12 Riley C. Walter, Attorneys for Debtor
13 Tulare Local Healthcare District, dba
14 Tulare Regional Medical Center
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